

No. 15924.

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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JACK J. WALLEY, Executor of the Estate of MURREY  
LONDON, Deceased,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

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On Appeal From the Judgment of the United States District  
Court for the Southern District of California.

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## APPELLANT'S REPLY BRIEF.

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### Preliminary Statement.

The arguments and authorities advanced and cited by appellee are, for the most part, the same arguments and authorities advanced and cited by the trial court in its opinion in support of its judgment. Those arguments were answered and the authorities analyzed by appellant in his opening brief and therefore will not again be referred to in this Reply Brief. Appellant will content himself with an analysis, of the new cases cited by appellee and the intent and purpose of the Bankruptcy Act, as evidenced by the provisions thereof and the decisions of the courts in which the provisions are interpreted and construed.

## Appellant's Reply.

The Bankruptcy Act in essence provides a proceeding whereby an insolvent person, firm or corporation may be discharged from payment of its obligations by turning over to the bankruptcy court all of its assets, not exempt by law, for distribution to its creditors. The Trustee in Bankruptcy does not represent the bankrupt, who generally has his own counsel, but represents the creditors, and is under a duty to obtain for the benefit of the creditors all of the assets of the bankrupt; disclosed, concealed and conveyed away to some creditors as preferences. The position of the Trustee, obviously is, in some instances, adverse to the interests of the bankrupt. Claims filed by creditors are not filed for the purpose of litigating and reducing to judgment the bankrupt's obligations, but are filed by creditors for the purpose of sharing in the assets of the bankrupt's estate.

Section 2(a) of the Bankruptcy Act, relating to the creation of courts of bankruptcy and their jurisdiction, sets forth various things that the court is required to do in the administration of a bankrupt's estate; it provides in Subdivision (2) that the court shall allow claims, disallow claims, reconsider allowed and disallowed claims, and after reconsideration allow or disallow them *against bankrupt estates*; it provides in Subdivision (3) that the Receiver in Bankruptcy shall be authorized to prosecute or defend suits by or against a bankrupt in behalf of the estate, but only when the court is satisfied it is necessary *to preserve the estate or to prevent loss thereto*; and it provides in Subdivision (7) the court shall cause the estate to be collected, reduced to money and distributed to the creditors and in connection therewith *to determine*

*controversies in relation to the collection and distribution of such estates.*

Section 7(a) of the Act, respecting the duties of bankrupts, provides as follows: In Subdivision (3), that they shall examine and report to the Trustee facts concerning the correctness of all proofs of claim *filed against the estate*; and in Subdivision (7) to report to the Trustee the falsity of any claim that may have been filed *against the estate*. It is further provided in said Section that if the bankrupt is required to attend at any examination *relating to the falsity of any claim or the correctness thereof*—other than as part of the first meeting of creditors—that he shall be paid his actual and necessary travelling expenses for any distance in excess of 100 miles from his residence to the place of the hearing.

It is provided in Section 14 of the Act that the bankrupt may waive his right to a discharge from his obligations so that his creditors may eventually, after having participated in the distribution of assets, proceed to enforce the obligation owing by the bankrupt. (Secs. 2, 7 and 14, Bankruptcy Act, Appendix, *infra*.)

It would appear from these provisions of the Act that it is the primary purpose, if not the only purpose, of bankruptcy proceedings, to provide a procedure by which an officer of the court, the Trustee, representing the creditors, shall marshal all of the assets of an insolvent person for the purpose of reducing them to money and distributing them, after payment of the expenses of administration, to the creditors entitled thereto, and in determining which of the creditors are entitled thereto to engage in litigation and to require the assistance of the bankrupt for that purpose. It would appear to follow that in determining the rights of the creditors, *to share*

*in the bankrupt's estate*, that in any such litigation, any order, decree or judgment made by the Referee or by the Bankruptcy Court, would be an adjudication between, and binding upon, the Trustee and the particular creditor, and in no wise an adjudication binding upon the bankrupt, not a party and not represented in the litigation. The imposition of a duty upon the bankrupt, to disclose to the Trustee the incorrectness or falsity of certain claims, and payment of his travel expenses, argues more strongly against, rather than in favor of, appellee's contention that this provision of the Act is for the benefit and protection of the bankrupt and gives him standing to object to such claim. The duty is imposed upon the bankrupt for the protection of the creditors, whom the Trustee represents, since it has for its purpose the preservation of assets for those creditors lawfully entitled to share therein. If the mere filing of a claim in bankruptcy, not dischargeable under the Act, had the effect of a judgment against the bankrupt, it would not be necessary to impose a duty upon the bankrupt to disclose false or incorrect claims, his own best interests would compel such disclosure and would be sufficient protection for the creditors lawfully entitled to share.

This construction of the intent and purpose of the Congress in enacting the Bankruptcy Act is borne out by the opinions in *Goldstein v. Pierson*, *In re McChesney* and *Massee & Felton v. Bennenson*, cited in Appellant's Opening Brief. In each of those cases, the court, in negating a similar contention of the government, took the position, (1) that the filing of a claim in bankruptcy was in no sense a claim *in persona* against the bankrupt; (2) that the Trustee in Bankruptcy represented the creditors and not the bankrupt, and could not bind him to a

personal judgment; and (3) that the filing of a claim and its allowance is in the nature of a petition to share in funds held by the court for distribution to creditors.

This view is not rejected by the Court of Appeals of the Second Circuit in *New York, N. H. & H. R. Co. v. Reconstruction Fin. Corp.*, nor by the Court of Appeals of the First Circuit in *Cohen v. United States*, cited in appellee's brief and so contended by the government.

In the *New York, N. H. & H. R. Co.* case the claim involved was a "secured claim" and in determining whether the allowance of a "secured claim" has the effect of reducing the claim to a judgment, the court considered the various provisions of the Bankruptcy Act. The court points out that *no order allowing a claim is necessary* since Section 57(d) of the Bankruptcy Act provides for allowance upon presentation to the court and therefore no order of allowance is required, *at least not unless objection is made* when the claim is first received or presented to the court. The court then goes on to say at page 245:

"How far the 'allowance' so provided has the effect of a judgment is by no means wholly clear; but for the purpose of the case at bar, we will assume that unsecured claims, when 'allowed' are to be considered as reduced to judgment."

The court then goes on to point out that on the other hand, Section 57(e) provides that "secured claims" shall be only temporarily allowed until the value of the security shall be appraised. The court then reasons:

"Thus there could not be 'final allowance' of the claim in suit until the amount of the security has been appraised."

It is quite evident that the claim, made by the government in its brief, that the decision in the above case establishes the principle that *the allowance of an unsecured claim without any objection or contest reduces the claim to a judgment against the bankrupt*, is without support. The statement made by the Circuit Court was that it was not at all clear whether the allowance of an unsecured claim has the effect of a judgment and that the assumption would be made only for the purpose of argument. In addition the statement was purely obiter dictum since the claim involved in that case was a *secured claim* and the statement was not necessary to an adjudication of the issue there involved.

The claim made by the government that the First Circuit, in *Cohen v. United States*, 115 F. 2d 505, establishes the principle, that, a tax claim filed in bankruptcy has the effect of a judgment against the bankrupt, although allowed without objections or other contest of the claim, is not supported by the decision in that case. Moreover the quoted portion of the decision, contained in appellee's brief, to wit: "This was a final adjudication of the tax claim . . .", is not a correct quotation, omitting, as it does, a portion of the opinion joined by the conjunctive "and." The portion of the opinion to which the government refers provides as follows:

"This was a final adjudication of the tax claim *and was conclusive against the Trustee.*"

*Cohen v. United States* was an action brought by a Trustee in Bankruptcy against the United States to recover overpayment of taxes made by the Trustee in due course of administration of a bankrupt estate. It does not appear from the facts recited in the opinion whether the tax claim was filed with the clerk of the court and

allowed automatically, or whether an order of the Referee allowing the claim, was made after objections interposed by the Trustee, at the time of its filing with him. An examination of the facts in the opinion of the District Court, *32 Fed. Supp. 1*, indicates that the Order of Allowance was made by the Referee apparently after objections made to the filing of the claim. Amongst other things it is pointed out in the opinion that the Trustee failed to petition for a review of the Order of the Referee.

Of more importance than the question as to whether the allowance was a formal one following the mere fact of filing, or whether the allowance was one made after objection, is the decision of the Circuit Court that the Order of the Referee is an adjudication *binding upon and conclusive as to the Trustee*, not the bankrupt.

The First Circuit relied upon the decision *In re Universal Rubber Products Co.* (1928), 25 F. 2d 168, affirmed by the Third Circuit in 28 F. 2d 255.

In that case, the government filed a tax claim in the bankruptcy proceedings; the Trustee paid a part thereof and then petitioned the Bankruptcy Court for an order disallowing the balance; a show cause order was served upon the government and upon its failure to appear or file any petition, the Referee, on December 1, 1925, made an order disallowing the excess. About a year later the Trustee filed a petition for disallowance of a portion of the tax claim already allowed and paid and for a refund thereof. The government appeared in response to this second petition and contested the petition for refund and filed its own petition for an amendment of its claim. An order made by the Referee granting the petition of the Trustee was reversed by the District Court. It was held by the court that the facts did not

justify the granting to the Trustee of the relief which he sought under the second petition, and said the court:

“We believe that the order of December 1, 1925, was a final adjudication of this tax claim and that it is conclusive both against the Trustee in Bankruptcy who asked that it be entered, and against the collector against whom it was entered without appeal.”

It is significant that *Cohen v. United States* depends for support upon a case in which the Order of the Referee was made on a petition for disallowance, of a portion of a tax claim in a bankruptcy proceeding. However, what is more significant is the fact that in both the *Cohen* and the *Universal Rubber Products* cases, it was held by the respective courts that the orders, of allowance or disallowance, made by the Referee in each of the cases, was a final adjudication and conclusive *only as to the Trustee and the government*.

Appellant submits that these decisions are not inconsistent with the position taken by the courts in *Goldstein v. Pierson*, *In re McChesney*, and *Massee & Felton v. Bennenson*, but in fact support the decision in those cases,

“that any order of allowance of a tax claim, is at best an adjudication of the government’s rights to participate in a distribution of the assets of the estate, and does not constitute a personal judgment against the bankrupt”

and thus collectible without limitation as to time.

Of further significance is the fact that the First Circuit in *Cohen v. United States* relied in part for its decision upon *In re Anderson*, 279 Fed. 525 (1922), 2d Circuit. In that case the Trustee in Bankruptcy had the Referee issue an order to show cause against the Collector of

Internal Revenue to require him to appear and file his claim for taxes, due from the bankrupt, in the bankrupt's estate so that the Trustee could object and have a hearing thereon. The Collector appeared in response to the order to show cause but refused to file a claim, following which the Referee made an order barring the government *from participation in the estate* for any taxes for the year involved. This order was affirmed on appeal.

In its opinion the court states that the United States must file its claim for taxes, as any other creditor, *if it desires to share in the estate*, and that the court must determine any question, as to amount or legality of the tax, which might be raised by the Trustee. It is pointed out by the court that Section 64 of the Bankruptcy Act relating to debts which have priority, provides a procedure whereby the Bankruptcy Court may determine and adjudicate the amount and legality of a tax claim of the United States respecting its right *to share in the assets of the estate in preference to other creditors* and that any such adjudication *is binding upon the government and the Trustee*. The Trustee being charged with the duty of ascertaining and paying claims due the United States, whether filed or not, must have a speedy method for ascertaining the amount due the government as a prior claim in order that the Trustee discharge his responsibility.

Appellant does not contend, as the government would have the court believe, that a valid tax claim found to be legally due and owing by a bankruptcy court and conceded valid by a bankrupt taxpayer, can only become a judgment if an unwarranted objection is filed thereto pursuant to which an order is made. (Br. p. 10.) To so argue would indeed be absurd.

Appellant does contend that the mere filing of a tax claim, by the government, does not make it a valid tax claim; nor is it, by reason of its mere filing, found to be legally due and owing by the bankruptcy court, and conceded to be valid by the bankrupt taxpayer. Appellant contends that it is the Order of Allowance made by the court or Referee, after a hearing on objections or a petition for disallowance, that renders the tax claim valid and that results in an adjudication by the bankruptcy court that the tax claim is legally due and owing.

Nor can it be said that an objection or petition for disallowance, to the filing of the tax claim, is unwarranted, until such time as the court or Referee adjudicates it to be such, after the issue has been raised by the objection or the petition for disallowance filed thereto. If this contention on the part of appellant be absurd, then so are the decisions of the District Courts in the cases of *In re McChesney*, *Goldstein v. Pierson*, and *Massee & Felton v. Bennenson*, since the contentions made by appellant are not original but merely set forth the reasoning and decisions made by the courts in those cases.

So also would be the decision of the Circuit Court in *Lewith v. Irving Trust Co.*, since in that case it was also held by the court:

“ . . . But allowance after objection . . . is another matter; there has been a litigation upon issues settled by the decision of the Court. Such an allowance has the substantial element of a judgment and has the effect of a judgment . . . ”

Respectfully submitted,

MILTON DAVIS,

*Attorney for Appellant.*





## APPENDIX.

### BANKRUPTCY ACT OF JUNE 22, 1938:

Sec. 2: Creation of Courts of Bankruptcy and their Jurisdiction.

(a)(2): Allow claims, disallow claims, reconsider allowed or disallowed claims, and allow or disallow them *against bankrupt estates*;

(3) Appoint, upon the application of parties in interest, receivers or the marshals to take charge of the property of bankrupts *and to protect the interests of creditors* after the filing of the petition and until it is dismissed or the trustee is qualified; and to authorize such receiver, upon his application, to prosecute or defend any pending suit or proceeding by or against a bankrupt or to commence and prosecute any suit or proceeding in behalf of the estate before any judicial, legislative, or administrative tribunal in any jurisdiction, until the petition is dismissed or the trustee is qualified: *Provided, however,* That the court shall be satisfied that such appointment or authorization *is necessary to preserve the estate or to prevent loss thereto*;

(7) Cause the estate of bankrupts to be collected, reduced to money and distributed, *and determine controversies in relation thereto*, . . .

### Sec. 7. Duties of Bankrupts.

a. . . (3) examine and report to his trustee concerning the correctness of all proofs of claim *filed against his estate*; (7) in case of any person having to his knowledge proved a false claim *against his estate*, disclose that fact immediately to his trustee; (10) . . . : *Provided, however,* that when the bankrupt is required to attend for

examination, except at the first meeting and at the hearing upon objections, if any, to his discharge, he shall be paid actual and necessary travelling expenses for any distance in excess of one hundred miles from his place of residence at the time of bankruptcy: . . .

Sec. 14: Discharges, When Granted:

a. The adjudication of any person, except a corporation, shall operate as an application for a discharge: *Provided*, That the bankrupt may, before the hearing on such application, waive by writing, filed with the court, his right to a discharge. (Italics supplied throughout.)